MOODY'S INVESTORS SERVICE

CREDIT OPINION
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Johnson (County of) KS

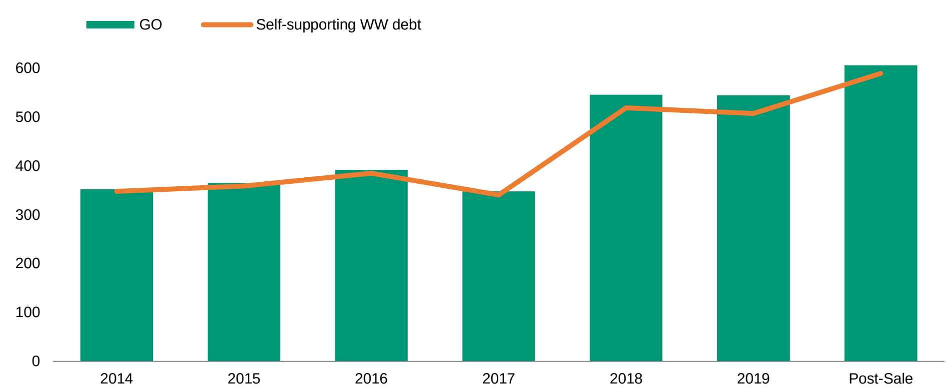
Update to credit analysis

Summary

The credit profile of Johnson County, KS (Aaa stable) benefits from the county's sizeable and wealthy tax base that serves as a major employment center in the Kansas City metropolitan area, well-managed finances with healthy reserves, and low net direct debt (exclusive of self-supporting wastewater general obligation debt) and pension burdens. These attributes are weighed against the county's elevated fixed costs inclusive of public building commission (PBC) debt service and a modest concentration in the telecommunications industry.

We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. We do not see any material immediate credit risks for Johnson County given the county's long-term trend of well-managed finances and maintenance of healthy reserves. However, the situation surrounding coronavirus is rapidly evolving and the longer term impact will depend on both the severity and duration of the crisis. If our view of the credit quality of the county changes, we will update our opinion at that time.

Exhibit 1
Nearly all county general obligation debt supported by wastewater enterprise
(Left axis in millions)



Source: Johnson County audited financial statements, Moody's Investors Service

Credit strengths

» Very large, wealthy, and growing tax base that serves as an employment base for the broader Kansas City metro area

» Well-managed finances with healthy reserves

» Low net direct debt and pension burden

Credit challenges

» Elevated fixed costs inclusive of public building commission debt service

» Modest concentration in the telecommunications industry

Rating outlook

The stable outlook reflects our expectation that the county's financial position will remain stable relative to revenues, supported by strategic budgeting practices and a strong underlying economy.

Factors that could lead to an upgrade

» Not applicable

Factors that could lead to a downgrade

» Trend of declining general fund reserves to a level inconsistent with the rating category

» Significant erosion of the county's tax base and resident income levels

» Failure to properly manage the county's wastewater fund leading to less than sum sufficient debt service coverage, and tax base support for wastewater capital projects and debt

Key indicators

Exhibit 2

Johnson (County of), KS	2015	2016	2017	2018	2019
Economy/Tax Base					
Total Full Value ($000)	$63,338,502	$67,091,395	$71,258,958	$76,464,420	$82,057,372
Population	566,814	572,428	578,797	585,502	602,401
Full Value Per Capita	$111,745	$117,205	$123,116	$130,596	$136,217
Median Family Income (% of US Median)	143.7%	144.3%	143.7%	142.6%	142.6%
Finances					
Operating Revenue ($000)	$284,579	$309,617	$311,834	$328,920	$341,306
Fund Balance ($000)	$68,247	$78,662	$87,165	$93,690	$101,958
Cash Balance ($000)	$73,616	$83,953	$95,367	$96,887	$116,469
Fund Balance as a % of Revenues	24.0%	25.4%	28.0%	28.5%	29.9%
Cash Balance as a % of Revenues	25.9%	27.1%	30.6%	29.5%	34.1%
Debt/Pensions					
Net Direct Debt ($000)	$272,787	$285,913	$304,094	$415,930	$404,242
3-Year Average of Moody's ANPL ($000)	$510,511	$535,524	$563,307	$597,522	$630,785
Net Direct Debt / Full Value (%)	0.4%	0.4%	0.4%	0.5%	0.5%
Net Direct Debt / Operating Revenues (x)	1.0x	0.9x	1.0x	1.3x	1.2x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.8%	0.8%	0.8%	0.8%	0.8%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.8x	1.7x	1.8x	1.8x	1.8x

Source: Johnson County's audited financial statements fiscal years 2015-19; US Census Bureau

Profile

Johnson County encompasses 477 square miles in the southwestern portion of the greater Kansas City metro area and is home to approximately 602,000 residents. The pubic building commission is a municipal corporation created in 1990 for the benefit of the county and its residents, including planning, development, construction, furnishing and equipping of public buildings for the benefit and use of the county. It is a component unit of the county, and is governed by the seven members serving on the county board of commissioners.

Detailed credit considerations

Economy and tax base: large, affluent tax base benefits from significant role in Kansas City metro area economy

The coronavirus is driving an unprecedented economic slowdown. We currently forecast US GDP to decline significantly during 2020 with a gradual recovery commencing toward the end of the year. Local governments with the highest exposure to tourism, hospitality, healthcare, retail, and oil and gas could suffer particularly severe impacts. The effect on local governments will vary based on the extent and duration of local disruption and could be more or less severe than the nation overall. The evolution of the crisis remains highly uncertain and the full extent of the economic costs will be unclear for some time.

The county serves as the economic engine for the state, and is positioned to remain in expansion mode given the strength of the underlying economy and steady demand for residential and commercial property. Over the past five years, the county's full valuation increased 6.6% on average, including a 4.6% increase for fiscal 2020 to $85.8 billion. The county's preliminary fiscal 2021 valuation indicates growth of 5.25%, however, management expects limited moderation prior to finalization of the assessed values in October. The tax base is diversified, though there is modest workforce concentration in the telecommunication industry. Management anticipates continued tax base expansion of 4-6% annually over the near term.

Similar to the rest of the nation, the county's unemployment rate skyrocketed in response to the coronavirus pandemic and resulting economic shutdown. However, the county's May 2020 unemployment rate of 9.3% fared better than both state (9.8%) and national (13%) levels for the same period, a further indication of the strength of the county's economy. The county's strong resident income indices (median family income equals 142.6% of the US) will also buoy the local economy during this period of economic uncertainty.

Financial operations and reserves: stable, well-managed financial operations with maintenance of healthy reserves

As a result of the pandemic, county revenues are expected to see some decline in fiscal 2020 and into fiscal 2021, however, strong assessed valuation growth and a healthy increase in the collection of use taxes (sales tax for online purchases) which somewhat mitigates the decline in brick-and-mortar retail collections, will provide stabilization. The county's five year general fund forecast anticipates modest planned drawdown for one-time expenditures in fiscal 2021; reserves are anticipated to remain in excess of $100 million through fiscal 2025.

Conservative budgeting practices produced a $17 million general fund surplus in fiscal 2019 as revenues performed better than anticipated and expenditures were flat year over year. The surplus improved available general fund reserves to $99.3 million, representing 29.4% of revenues. Going forward, we expect to see a general fund balance stabilizing around the 25% level at a minimum; county policy is to maintain reserves of at least 20-25% of expenditures. The available balance in the debt service fund is relatively small, though adequate considering most of the GO debt is supported by enterprise funds. In addition to the general and debt service funds, $19.5 million of the balance in the capital projects fund is also legally available liquidity to fund general operations if needed.

The county's fiscal 2020 budget included a $5 million draw to fund election expenses and capital. Current estimates indicate a $15 million impact to county revenues relative to the budget, primarily attributable to reduced sales tax collections and investment income. To offset the potential revenue impact, management identified $25 million in contingent expenditure savings primarily through vacancies and the deferral or reduction of capital spending. Relative to the county's estimates at the beginning of the coronavirus pandemic, actual performance has improved monthly. If revenue performance continues to improve the county may not implement the full slate of reductions.

Conservatively, none of the county's projections include utilization of the $116.3 million received from the CARES Act funding. Officials plan to utilize a portion of the funding to offset expenditures for public health and safety salaries, testing supplies, personal protective equipment, and other contractual and commodity expenses incurred in response to the pandemic. The county will also provide a portion of the funding to municipalities in the county that incurred coronavirus related expenditures; funding not utilized by December 31 must be returned to the federal government.

The county's primary revenue source is property taxes which accounted for 68% of fiscal 2019 general governmental revenues with sales tax revenue providing roughly 27%.

LIQUIDITY

The county closed fiscal 2019 with $116.5 million in operating liquidity, comprised of $113.7 million in general fund and $2.8 million in debt service liquidity. Operating liquidity represented a healthy 34.1% of operating revenues.

Debt and pensions: low direct debt burden due to material support from essential wastewater enterprise; manageable pensions

The county's net direct debt burden will remain low as the burden on the tax base is largely offset by support from the wastewater enterprise. Of the county's $606.2 million of general obligation debt, $589.5 million is supported by wastewater revenues and is backed out of the calculation. The net direct debt burden also includes $321.1 million in lease revenue bond debt issued through the Public Building Commission (PBC); the PBC debt is secured by the county's general fund revenues and is not subject to annual appropriation. All in net direct debt represents a low 0.4% of the fiscal 2020 full value of the tax base.

The county's five year capital improvement plan calls for nearly $900 million in capital investments, nearly half of which is dedicated to wastewater projects, the majority of which will be debt funded. County policy is for wastewater capital charges and user fees to maintain 1.1 times debt service coverage on the wastewater general obligation debt; though the county targets and typically exceeds 1.2 times coverage. The county has projected regular rate increases ranging from 5%-7% annually through 2027 to maintain debt service coverage of at least 1.2 times.

DEBT STRUCTURE

All of the county's debt is fixed rate and matures over the long-term (final maturity in fiscal 2040). Amortization is slower than the median with 52.5% general obligation debt and 90.7% of PBC lease revenue debt retired within ten years.

DEBT-RELATED DERIVATIVES

The county is not party to any interest rate swaps or other derivative agreements.

PENSIONS AND OPEB

Budgetary pressure is expected to remain manageable from the county's exposure to two statewide cost-sharing plans, the Kansas Public Employees Retirement System (KPERS) and the Kansas Police and Fireman's Retirement System (KP&F). Both plans are administered under KPERS, and county has consistently made its statutorily required contribution to both plans. In fiscal 2019, the county contributed $25.3 million to the pension plans, net of the estimated $703,000 in contribution from the wastewater fund. The contribution represented 7.4% of operating revenues. Moody's three-year adjusted net pension liability (ANPL) for the county, under our methodology for adjusting reported pension data, is $630.8 million, equal to a modest 1.8 times operating revenues and 0.8% of full value.

The county's fixed costs are somewhat elevated, largely driven by PBC and self-supporting wastewater general obligation debt service. As of 2019, total general obligation and lease revenue debt service equated to $88.7 million, or 26% of operating revenues (general and debt service fund), which does not include any charges for services revenues within the wastewater or public building commission that may be used to offset debt service. Were wastewater and PBC revenues included, fixed costs related to debt service would fall to a more manageable 17.1% of combined revenues. Inclusive of pension and OPEB contributions, total fixed costs totaled 32.5% of operating revenues, or 21.3% inclusive of wastewater and PBC revenues.

The county's fiscal 2019 contribution exceeded the “tread water” level by about $4.4 million. The “tread water” indicator is a measurement that indicates whether contributions are sufficient to prevent the unfunded liability from growing, under reported assumptions. It is calculated as the normal cost plus interest on the unfunded liability at the assumed rate of return; in 2017 KPERS reduced the discount rate to 7.75% from 8%.

The county offers other post-employment retirement benefits (OPEB). As of 2019, the OPEB liability was small at $29.5 million, or 0.1 times operating revenues.

ESG considerations

ENVIRONMENTAL

Environmental considerations do not present material risks to the county's credit profile. The county's location in eastern Kansas (Aa2 stable), along the border with Missouri, puts it at high and medium risk for heat and extreme rainfall, respectively. Extreme weather events are also typically accompanied by state and federal assistance, which further mitigates environmental risk.

SOCIAL

Please see the “Economy and tax base” section above for more detail on social considerations.

GOVERNANCE

Fiscal management of the county is strong and forward-looking, evidenced by the willingness and ability to cut expenses as needed, maintain healthy reserves and execute long-range financial plans.

Kansas counties have an institutional framework score of “Aaa,” which is high compared to the nation. Counties rely heavily on property tax revenues, which are highly predictable. Local option sales taxes are a smaller revenue source. Counties enjoy a strong ability to increase property taxes without limit. In 2018, a new state law limited property tax revenue increases without voter approval, though the legislation includes numerous exemptions, resulting in a moderate revenue-raising ability. Expenditures mostly consist of public safety, which are highly predictable. Counties have a high ability to reduce major expenditures given the lack of collective bargaining units in most of the state.

Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 3

Johnson (County of), KS

Scorecard Factors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$85,845,760	Aaa
Full Value Per Capita	$142,506	Aa
Median Family Income (% of US Median)	142.6%	Aa
Notching Factors:[2]		
Regional Economic Center		Up
Finances (30%)		
Fund Balance as a % of Revenues	29.9%	Aa
5-Year Dollar Change in Fund Balance as % of Revenues	9.6%	A
Cash Balance as a % of Revenues	34.1%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	12.8%	Aa
Management (20%)		
Institutional Framework	Aaa	Aaa
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures (x)	1.0x	Aa
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	0.4%	Aaa
Net Direct Debt / Operating Revenues (x)	1.1x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	0.7%	Aaa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.8x	A
	Scorecard-Indicated Outcome	Aaa
	Assigned Rating	Aaa

[1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.
Source: Johnson County's audited financial statements fiscal years 2015-19; US Census Bureau

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